



# Memorandum

**TO:** CITY COUNCIL

**FROM:** Mayor Chuck Reed

**SUBJECT: MARCH BUDGET MESSAGE  
FOR FISCAL YEAR 2010-2011**

**DATE:** March 12, 2010

Approved:

Date:

3/12/10

## **RECOMMENDATION**

I recommend that the City Council direct the City Manager to submit a proposed budget for Fiscal Year 2010-2011 that is balanced and guided by the policy direction and framework of priorities outlined in the Mayor's March Budget Message. Proposals for budget reductions should provide detailed analysis of their feasibility including in-depth data, justification, and outcomes for the City Council to consider later this spring.

## **INTRODUCTION**

Economists and financial experts believe that the deep recession of 2009 may be over, and there seems to be a renewed optimism that a national economic recovery is underway. Positive growth is anticipated for 2010-2011 based on recent data on consumer spending, business investment, and the outlay of federal stimulus dollars. This is good news of course and I am hopeful that the impacts of a recovery will result in positive outcomes for our city in 2010.

The realities of our present situation, however, are grave. The impacts of the financial crisis have been particularly severe on the Silicon Valley as highlighted at the State of the Valley 2010 by Joint Venture Silicon Valley and by our staff at the February 8, 2010 Study Session on the Economic Strategy Update 2010-2015. City revenues have experienced significant declines in the last two years and, in a number of cases, are not expected to reach pre-recession levels for many years. At the same time, city retirement costs are expected to rise substantially, primarily to account for huge investment losses sustained during the economic downturn and changes in actuarial assumptions.

These realities are reflected in the General Fund shortfall of \$116.2 million projected for 2010-2011 as detailed below.

### General Fund 2010-2011 Shortfall

2010-2011 Shortfall Component	\$ in Millions
<b>Expenditure Changes</b>	
Increased Retirement Contribution Rates (estimate) (Police/Fire Plans: \$43.6 million; Federated Plan: \$9.3 million)	(\$52.9)
-Increased Expenditures (primarily personnel-related)	(\$10.2)
-2010-2011 Committed Additions (new Police Officers/facilities)	(\$7.5)
-Carry-over from 2009-2010 Adopted Budget	(\$3.1)
<b>Sub-Total Expenditure Changes</b>	<b>(\$73.7)</b>
<b>Decreased Revenue Estimates</b>	<b>(\$42.5)</b>
<b>Total 2010-2011 Projected General Fund Shortfall</b>	<b>(\$116.2)</b>

Source: 2010-2011 City Manager's Budget Request and 2011-2015 Five-Year Forecast and Revenue Projections issued in February 2010

From past experience, combined with current trends, we can assume that:

- Next year will be extremely challenging for the City of San José, and the impacts from the economic recession will continue to linger in 2010-2011.
- The economic recovery will be gradual.
- Because government revenue sources do not track directly with the rest of the economy, revenue improvements will lag behind overall economic growth.

### Economic Conditions

The severity and longevity of the current economic downturn has caused continued declines in many of the City's largest and most critical revenues. Instability in the financial markets, declining home values and increasing foreclosures, and rising unemployment have hit all of our major revenues streams hard.

A comparison of the performance of economically sensitive major revenues for our General Fund, special funds, and capital funds by our Budget Office staff in February of this year found declines in all categories in 2009-2010 compared to the peak, including property tax (-5%), sales tax (-26%), Transient Occupancy Tax (TOT) (-41%), development fee programs (-39%), and airport passenger facility charges (-26%) as summarized in the following table. It should be noted that the amounts shown do not reflect adjustments for inflation.

**Comparative Performance of Economically Sensitive Major Revenues**  
(\$ in millions)

Revenue Source	Peak		Actual		Modified Budget*	% Decline from Peak	
	Year	Actual	2007-08	2008-09	2009-10	2008-09	2009-10
Property Tax	2008-09	\$ 210.84	\$ 203.72	\$ 210.84	\$ 199.85	0.0%	-5.2%
Sales Tax	2000-01	169.22	154.00	132.01	125.08	-22.0%	-26.1%
Transient Occupancy Tax	2000-01	27.61	24.03	19.35	16.38	-29.9%	-40.7%
Development Fee Programs**	2005-06	41.21	38.20	31.92	25.19	-22.5%	-38.9%
Airport Parking and Roadway Rev.	2000-01	60.01	48.01	42.60	38.71	-29.0%	-35.5%
Airport Passenger Facility Charges	2005-06	22.27	21.22	17.42	16.50	-21.8%	-25.9%
Construction and Conveyance Tax	2005-06	49.00	26.81	20.47	20.00	-58.2%	-59.2%
Construction Excise Tax***	2000-01	20.74	13.55	8.12	5.50	-60.9%	-73.5%
Building and Structure Const. Tax***	2000-01	17.45	9.62	7.05	4.00	-59.6%	-77.1%
Sanitary Sewer Connection Fee	1997-98	2.70	0.79	0.65	0.25	-75.9%	-90.7%

\* Modified Budget based on revisions to revenue estimates approved in the 2009-10 Mid-Year Budget Review Report.

\*\* Development Fee Programs include Building, Fire, Planning, and Public Works.

\*\*\* The 2009-10 budget includes valuation table increases.

Property tax is the largest source of revenue for the General Fund. When real estate values drop, the Santa Clara County Assessor issues lower assessments, which results in lower property tax revenue for the city. For the 2009-2010 property tax assessment roll, over 52,000 properties received downward adjustments from the Santa Clara County Assessor based on the decline in property values. In 2010-2011, collections are expected to drop an additional 1.1 percent to \$199.1 million, primarily reflecting the California Consumer Price Index change (which was a decrease of 0.237 percent) and an anticipated drop in commercial valuation.

Sales Tax and Transient Occupancy Tax (TOT) receipts have also been significantly impacted by the severe economic downturn. In 2008-2009, Sales Tax collections of \$132 million reflected a decline of 14.3 percent (down \$22 million) from the 2007-2008 level. In 2009-2010, an additional decline of 5.5 percent (\$7.3 million) is expected. In 2010-2011, Sales Tax receipts are expected to increase a modest 2 percent. In the Transient Occupancy Tax category, receipts declined 18.5 percent in 2008-2009 and are expected to fall an additional 15.9 percent in 2009-2010. In 2010-2011, slight growth of 2 percent is projected.

### **Other Challenges**

#### **State of California**

The most significant risk to the revenue forecast is the magnitude of the State of California's budget deficit. Many of the City's most critical revenue sources – sales taxes, gasoline taxes, vehicle license fees, and others – pass through the state coffers before being disbursed to the City. Over the past 12 years, the State of California has taken more than \$500 million from San José. This has resulted in an ongoing annual loss of revenue of \$42.8 million as shown in the following chart.

**Major State Budget Actions on General Fund  
(FY 1990-1991 through 2009-2010)**

Action Description	Cumulative Cost or Revenue Loss to the City	Annual Cost or Revenue Loss to the City
Allowed County to charge cities for property tax collection	\$23,396,000	\$2,619,000
Diversion of cigarette tax	\$25,349,000	\$1,368,000
Allowed County to charge cities for booking prisoners at County jails (restored in 1999-2000, rescinded in 2005-2006, payments between County and State starting in 2007-2008; payment to County reduced 10% by State in 2008-2009 City subject to reimbursing county)	\$30,745,000	
Withdrew half of vehicle citation fees (restored in 1998-1999)	\$7,700,000	\$0
ERAF property tax shift	\$438,075,000	\$39,056,000
Elimination of County's Animal Control Program (program shifted to City in 1993-1994)	\$58,383,000	\$3,527,000
Proposition 172-public safety sales tax	-\$68,412,000	-\$3,725,000
Motor vehicle in-lieu tax diversion (2003-2004)	\$846,000	\$0
San José contribution to State (2004-2005 & 2005-2006)	\$22,198,000	\$0
<b>Total</b>	<b>\$538,280,000</b>	<b>\$42,845,000</b>

In addition, in 2009-2010 and 2010-2011, the state plans to take a total of \$75 million from the Redevelopment Agency. This will take funds from San José that are needed for projects to revitalize neighborhoods throughout the city and to stimulate our local economy. The California Redevelopment Association has sued the state and that litigation is moving forward.

**Pensions**

The City's pension plans are established by the City Charter. The City makes payments to the two pension funds and those payments are adjusted based on the performance of each pension fund to ensure we are able to meet our obligations to our employees and retirees. Due to the drastic drop in pension fund values, as well as changes in actuarial assumptions, early projections are that San José will need to increase City pension contributions by \$52.9 million in 2010-2011, which has significantly boosted the projected shortfall. As described in the City Manager's Forecast document, the contribution rates for our pension systems are also expected to increase dramatically over the next several years.

**Arbitration**

In 1980, San José voters approved a City Charter amendment requiring binding interest arbitration when the police and fire unions and the City reach impasse in labor negotiations. Since 1980, wages and benefits for our public safety unions have escalated faster than other labor contracts, faster than the City's overall revenues, and faster than other expenditures. With the Fire Department negotiations likely headed to arbitration, authority over wage and benefit

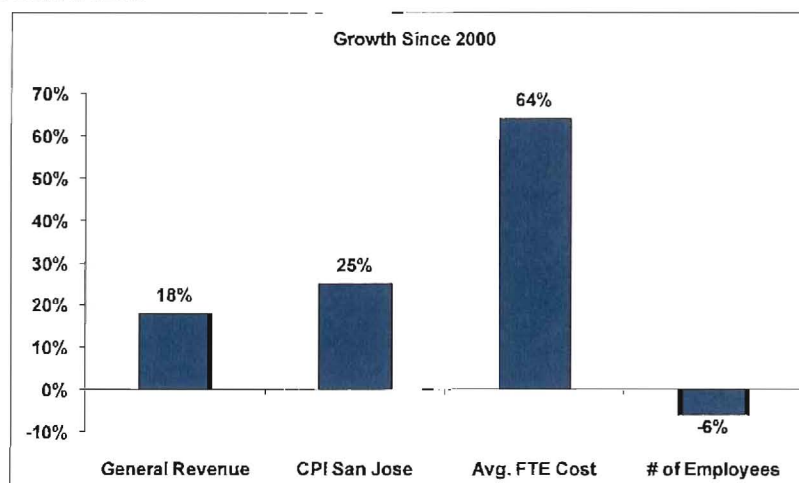


increases will be given to an outside party and any potential arbitration decision may impact our deficit.

In addition to the significant one-time costs of the arbitration process itself, an arbitrator can impose both short-term and long-term liabilities on taxpayers with no ability for the City to appeal the binding decision. In two instances, arbitrators have awarded increases in pension benefits to existing employees that immediately created significant unfunded liabilities that must be paid by future taxpayers. The first was in 1996 when an arbitrator increased the pension formula for police and fire. In 2007, an arbitrator awarded an enhanced 90 percent benefit to firefighters, but did not require them to fully fund retiree healthcare benefits as all other City employees are now doing. Given the City's fiscal situation and the need to reduce personnel costs to lessen reduction in services, hopefully arbitration can be avoided through the City Manager's continued efforts in negotiations with the police and fire unions that result in pension reform and personnel cost savings at least as much as is being asked of other City employees.

### **Expenses Growing Faster than Revenues**

Since Fiscal Year 2001-2002, we have eliminated over 880 full-time positions from our workforce, yet our expenses continue to grow. Salary increases are not the sole cause of increasing costs for services; other factors include rising healthcare and retirement costs. Expenses have grown faster than revenues for years. As displayed in the chart below, the average cost per employee



has gone up by 64 percent over the last nine years while revenues have gone up by only 18 percent. The net result is that we have been forced to cut employees and reduce services to balance our budget.

### **Reducing the Budget Deficit**

The City Charter requires that we have a balanced budget. Given the economic realities that I described earlier, it means we are faced with having to balance a \$116 million General Fund deficit. The questions we have to answer are: do we deeply slash services, show hundreds of workers the unemployment line, or look for other alternatives?

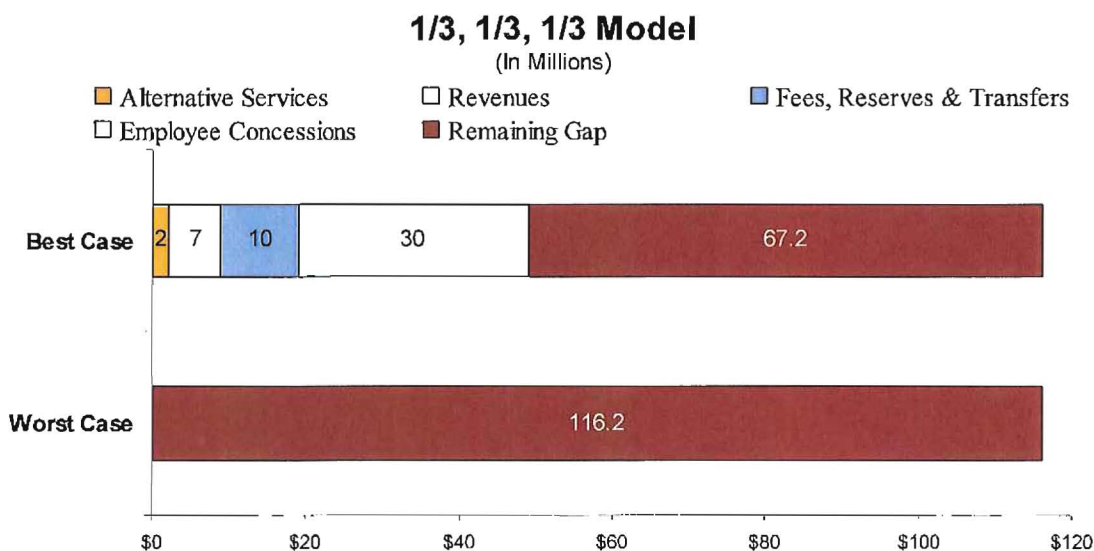
In November of last year, the City Council targeted closing the deficit equally from three areas:

- Employee wage and benefit concessions
- Revenues
- One-time revenues and alternative service delivery proposals and efficiencies in operations (with a request to refrain from using one-time revenues for budget balancing,

and instead use them for one-time needs, and to consider renegotiating existing service contracts to reduce costs)

If any portion could not meet the target, the default response would be to reduce services and eliminate jobs. Given that this is the ninth year of deficits, our options for creating new revenue solutions that don't require voter approval and improving efficiencies are limited.

It was clear from the February 16 Study Session that after anticipated solutions totaling \$10 million in fee increases, use of reserves and transfers, only up to \$7 million may be achieved from new revenues, with \$2 million from efficiencies, and \$30 million through a 5 percent concession from our employees. The 1/3, 1/3, 1/3 option is not going to get us to \$116 million without massive layoffs. As displayed in the following chart, if no action is taken and we move forward with this option, the remaining deficit that we will be forced to resolve through service eliminations is \$67 million, which could mean over 500 position reductions. This, in my view, is unacceptable.



I propose that at least half of the deficit be covered by concessions to save jobs and avoid service cuts. The City Manager is directed to begin discussions with our employee groups to achieve concessions equaling a 10 percent ongoing reduction in total compensation costs. In my discussion with the city labor leaders, there is a clear concern that any and all concessions would be used to buy back public safety services. To the extent possible, concessions from non-sworn bargaining units should primarily be used to save non-sworn positions, and savings from the sworn bargaining units should primarily be used to save sworn positions.

It is also very important that public safety be involved and engaged in the concession discussion. Because more than 60 percent of the City's General Fund revenues are spent on public safety, obtaining zero concessions or reductions in public safety would mean that we would have to reduce the non-public safety departments by more than 50 percent to make up this year's shortfall.



There is a menu of options we can pursue with our employees and the City Manager is directed to make a good faith effort to pursue and discuss all of them with our employees, including:

- If every employee deferred step increases and contractually required raises, we could save \$7.1 million in all funds and \$4.9 million in the General Fund.
- If every employee conceded 10 percent, we could save up to 450 jobs in the General Fund alone.
- If our bargaining groups agree to medical benefit cost-containment strategies, we could save \$16.8 million in all funds.

**Savings From Reducing Per Employee Cost (in millions)\***

5%			10%			15%		
General Fund	Other Funds	Total Funds	General Fund	Other Funds	Total Funds	General Fund	Other Funds	Total Funds
\$31.95	\$11.18	\$43.13	\$63.90	\$22.36	\$86.26	\$95.85	\$33.53	\$129.39

\*It should be noted, however, that compensation reductions that directly affect wages will have an overhead reimbursement impact to the General Fund which will result in a lower net General Fund savings than the figures stated. Also, because the cost-recovery Development Fee Programs are budgeted in the General Fund, any compensation reductions to employee groups budgeted in those fee programs will be captured directly in those programs, which will also reduce the General Fund savings that can be applied to resolving the \$116.2 million projected shortfall.

\*\*In Fiscal Year 2010-2011, the average sworn position is estimated to cost \$181,970. The average non-sworn position is estimated to cost \$109,773. The average position citywide is estimated to cost \$133,195.

In order for the City Manager to incorporate personnel cost savings into the proposed budget, resolution to pending labor negotiations need to occur by early April. The City Manager should continue efforts to reach resolution with bargaining units in order to incorporate those savings into the Proposed Budget.

If the negotiation process with some bargaining units has not concluded by early April or if there are additional personnel cost-savings proposals that some bargaining units propose to save positions, the savings could still be used to save jobs that would be eliminated in 2010-2011. However, the City Council would need to take action to approve those changes in open session on or before June 22 when the Council will adopt the budget for next fiscal year. In order to allow sufficient public review pursuant to Sunshine requirements, a City Council memorandum will need to be released by June 8. Therefore, resolution of pending labor discussions will need to occur by June 3 in order for a City Council memorandum to be drafted and released by the June 8 deadline. These timeframes highlight the importance of timely decisions related to our personnel costs in order to lessen the reduction in City services and loss of City jobs.

By sharing the pain, we can save jobs. If we take action, we can move forward and get through this economic slump. This will require discipline, collaboration, and creativity. But we must remember that hundreds of jobs, families, and services are at stake.

## **BACKGROUND**

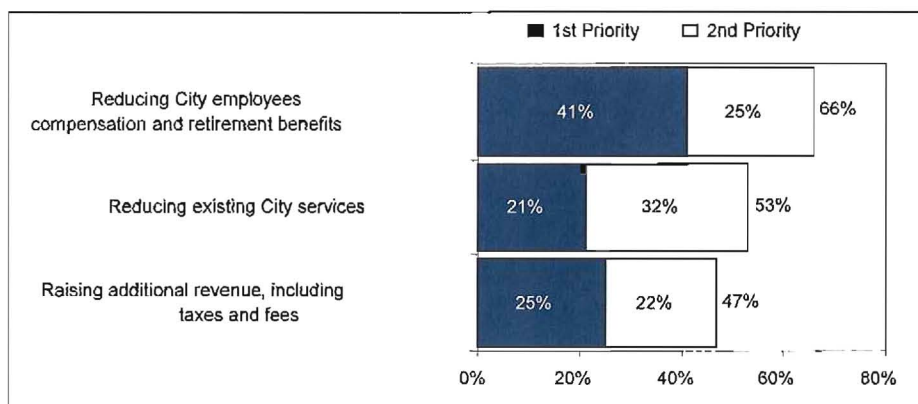
### **Neighborhood Views and Perspectives**

Four years ago, I proposed the Reed Reforms which included a new process for neighborhoods and residents to give input on the budget. Since then, community members have been actively involved in one of our most critical duties, developing the City budget.

I have worked closely with neighborhoods and the community to obtain input throughout the budget process. I held a Mayor's Budget Message Workshop to prioritize revenue options, and in January, we conducted a statistically valid community poll of our residents to get input on spending and budget priorities.

We convened neighborhood association leaders and members of the Youth Commission on January 23 to have an open dialogue about budget issues and priorities. In addition, as we have done the last two years, we will also hold budget meetings in each of the City Council Districts in March and April.

### **Preferred Approach to Balancing the Budget**



In the community survey, we asked residents how they preferred to balance the budget. The survey provided three strategies for addressing the shortfall – reducing City employees' compensation and retirement benefits,

reducing existing City services, and raising additional revenue, including taxes and fees. Residents were asked which strategy should be the City's highest priority. Forty-one percent of the residents polled stated that their first priority was for the City to first reduce employee compensation before reducing services or raising additional revenue.

### **New Revenues**

On December 17, 2009, I conducted a Mayor's Budget Message Workshop with community members and neighborhood leaders to discuss the potential revenue sources that require voter approval. Attendees discussed the pros and cons of each revenue source and proposed new revenue ideas. We were limited in the number of revenue ideas that we could include in our poll, so I asked residents to rank the revenue strategies. We included these revenue strategies in our community survey, and the results are in the chart below.



Polled Strategies	Survey Results	Potential Annual Revenue
Increase Card Room Tax and/or Number of Tables	64%	\$2M - \$5.3M
1/2 - 1/4 Cent Sales Tax Increase	48-53%	\$30.25M - \$60.5M
Disposal Facility Tax	43%	\$1.5M - \$8M
Modernizing Business Tax	43%	\$500k - \$13M
Parking Lot Tax	37%	\$5.2M - \$9M

The only two revenue strategies with a chance of getting voter approval are the card room tax increase and the ¼ cent sales tax increase. Sixty-four percent of likely voters would support an increased card room tax combined with an increase in the number of tables. At the March 9 City Council meeting, Council approved placing a proposal on the June ballot to increase the City's tax rate on gross revenues on card rooms from 13 to 15 percent, increase the number of tables from 40 to 49 at each of the two card clubs, allow any card game authorized under state law consistent with City regulations, and allow betting limits as authorized under state law.

Staff estimates that a ¼ cent sales tax increase would generate more than \$30 million per year in additional revenue. However, with the recent increase in the sales tax by the state of 1 percent bringing the Santa Clara County rate to 9.25 percent, support for a sales tax increase idea has decreased. Fifty-three percent of likely voters stated they would likely support a ¼ cent sales tax increase. There is still work to be done before City Council considers placing this item on the November ballot. One of the strongest arguments that would encourage voters to support a sales tax increase is to demonstrate that we have achieved concessions from our employees. A 10 percent reduction in pay and benefits would significantly increase public support. We also need to do more outreach to stakeholders who may be affected by and possibly oppose a sales tax measure. The City Manager is directed to work with my office to conduct additional analysis such as polling and outreach to stakeholders, and report back to City Council during the budget hearings.

### How Would You Spend Your Tax Dollars?

According to respondents from the budget survey, as well as input from the January 23 Session and online survey, San José residents prioritized their spending as follows:

#### HOW WOULD YOU SPEND A HUNDRED DOLLARS?



The budget needs to reflect the values of our community. It is clear from our community that a safe city is a priority. It is also clear that our community supports a balanced approach when it comes to spending their tax dollars.

### **Neighborhood Priorities for Reductions**

An important new component of the 2010 Community Survey was ranking specific proposals for reductions within the neighborhood services and public safety departments.

#### *Neighborhood Services*

The City Manager is directed to bring forward proposals for reductions within the Neighborhood Services City Service Area (CSA) that are consistent with neighborhood priorities. When considering budget proposals, reduction proposals should include more emphasis on reducing support for special events and park ranger support in regional parks. Consistent with the community's priorities, priority should be given to continuing sports and recreation programs, keeping as many community centers open as possible, providing therapeutic services for residents with mental illnesses, keeping park restrooms open to the greatest extent possible, and continuing anti-gang and at-risk youth programs to the greatest extent possible.

#### *Public Safety*

The City Manager is directed to bring forward proposals for reductions within the public safety departments that are consistent with neighborhood priorities, including:

- Deferring the opening of the South San José Police Substation.
- Reducing the number of police officers patrolling Downtown on horseback.
- Reducing hours dedicated to non-emergency community policing.

Consistent with the community's priorities, priority programs within public safety departments should include investigating violent crimes and assaults, maintaining resources to the extent possible dedicated to 9-1-1 emergency response times, investigating sexual assault crimes, and investigating homicides and murders.

### **GENERAL BUDGET GUIDELINES**

1. All proposals for either budget reductions or augmentations should be measured against the following criteria:
  - a. Impact on essential public services.
  - b. Adherence to Council-approved priorities.
  - c. Relative importance to operational efficiency.
  - d. Effect on fiscal integrity and flexibility.
  - e. Economic impact and jobs.

2. I recommend that the City Council approve the general budget-balancing strategy guidelines from the proposed 2010-2011 City Manager's Budget Request and 2011-2015 Five-Year Forecast and Revenue Projections document, as amended by this document.
3. The City Manager shall:
  - a. Develop a proposed budget that is balanced based upon our current revenue expectations and expenditure reductions.
  - b. Maximize reductions to ongoing programs to help solve future deficits to the fullest extent possible, and consider use of one-time funds when prudent.
  - c. Reductions that are personnel-related should primarily be ongoing cuts and not one-year freezes to better overcome future deficit projections.
  - d. Immediately coordinate and aggressively pursue opportunities for the City to apply for grants to support programs in priority areas.
  - e. Avoid budget cuts that could mean the loss of grants or our ability to leverage other resources.
  - f. With the exception of the Independent Police Auditor and the Redevelopment Agency, include all other Council Appointees' budget reduction proposals under the Strategic Support CSA for the May 1 proposed budget and include them in Budget Study Session discussions during the Strategic Support CSA.
  - g. Appointee and department reduction targets should not be met by shifting costs and other expenditures to departments or appropriations.
  - h. Initiate discussions with employee groups regarding any proposals that will be included in the proposed budget that may be subject to meet and confer.
4. To ensure overall strategic leadership and service delivery for the organization, the Mayor's Budget Office will work with the City Council Appointee offices to bring forward proposals that are equal to the average non-public safety CSA, with consideration given to service and operational impacts. Proposals for streamlining processes and enhancing the use of technology to improve operational efficiencies are to be proposed. Also, areas where duties can be modified so that the appointees can control workload to meet budgeted staffing levels are to be reviewed and proposed to Council. Reduction targets for Mayor and City Council Offices will be determined after consideration is given to service and operational impacts.

## **Investment Strategies**

### **1. Community and Economic Development**

The investment strategies that we employ over the next year will make a difference in whether we are able to successfully lead the City out of the fiscally stagnant position that it is in at the moment. Concentrating on our strengths and focusing on our economic development mission will help us maintain our position in the global economy as the world center of innovation.

According to the Milken Institute, San José/Silicon Valley ranks as the number one high-tech center in the U.S. Our businesses continue to innovate and invest in people, facilities and capital equipment. Productivity gains have been strong. Green technology companies have been registering patents at an increasing rate since the mid-'90s and Silicon Valley continues to be the most competitive and favored location for emerging companies and new business formation. We have opportunities like no other city in the world and must do everything we can to capture the gains that our region is bound to experience as the U.S. economy grows.

Now is the time to aggressively pursue our economic development goals to retain jobs, attract new companies, and offer our best capabilities in permitting projects that are in progress. Staff is currently engaged in advancing a number of initiatives approved by the Council, including the 2008 Economic Stimulus Plan, the Retail Strategy, the Green Vision, Redevelopment Plans in our Downtown, Industrial Areas, and Neighborhood Business Districts, the 2003 Economic Strategy, and land use development policies.

Of particular importance are the projects highlighted below:

- a. Economic Strategy Update 2010-2015:** The Economic Strategy Update 2010-2015 is being prepared for approval by the City Council in April 2010. At the February 8 Study Session, Council approved the Draft Economic Strategy presented by staff, as well as my recommendations to focus on four Strategic Goals and 10-15 Action Items as our highest priorities for implementation in 2010. It was also recommended that the best incentive we could afford our customers should be the delivery of permits at the speed of business.
- b. Convention Center Expansion and Renovation:** City Council has endorsed the renovation and expansion of the Convention Center as one of our best opportunities to effect short-term and long-term economic benefits and growth. City and Redevelopment staff are working with our partners at Team San José and the hoteliers to determine the scope of the Design-Build project, a timeline, and a funding strategy. The City Manager and Executive Director are directed to work with Team San José to develop an aggressive business development strategy to assure bookings of our existing facilities during construction, and commitments or statements of interest from event planners for the use of the new and expanded facilities after construction.
- c. Civic Auditorium:** City and Redevelopment staff along with Team San José are working on renovating this city landmark. At the February 23 Board Meeting, the Agency Board awarded phase two of this project to complete structural upgrades, add a



new ADA elevator, and build out concessions, (and other ADA improvements). However, the project will not be complete because it does not include fixed seating. The Executive Director is directed to report back on the completion of phase two, so that the Board can determine if there are project savings or identify other funds so the process for purchasing seats can be reinitiated.

- d. **Baseball:** In anticipation of a positive decision from Major League Baseball, staff is in the process of circulating a Supplemental EIR to support the development of a baseball stadium in Downtown San José. Infrastructure improvements to implement the goals of the Downtown Strategy Plan and the proposed construction of a stadium are also under way. The City Manager and Executive Director are directed to continue to make progress on their workplan.
- e. **Soccer:** A practice field for the San José Earthquakes on a two-acre site of the former FMC property is currently under construction. Plans are in progress to develop a permanent home for the Earthquakes. Staff is currently working on environmental review and rezoning of the site to accommodate an 18,000-seat professional sports stadium. The City Manager is directed to continue to work with the developer to deliver the permitting process in a timely manner.
- f. **Business Retention and Recruitment:** Redevelopment and City staff are aggressively courting and monitoring the growth plans of several driving industry and emerging technology companies, national retailers and international companies by providing site location assistance, permitting assistance, and business incentives as appropriate. This effort is being supplemented by a comprehensive array of services and programs offered by Work2Future, the downtown incubators, and the San José BioCenter.

Retaining and growing our tech companies, suppliers and service providers must continue to be a top priority in 2010. Redevelopment and OED staff have conducted 42 retention visits to driving industry companies between October 2009 and February 2010. As in my previous statements on this topic, I cannot reinforce enough how valuable this retention program is to our economic development mission. The City Manager and Executive Director are directed to develop a retention campaign for 2010 for the express purpose of meeting face-to-face with CEOs of at least 300 companies in San José. Councilmembers have, on many occasions, expressed their interest in making visits to CEOs. Now is the time to develop and implement a program around this effort.

- g. **Citywide Coordinated Marketing Effort:** Over the past year, the City Manager and the Executive Director have worked in partnership with the Mayor's Public Information Officer to coordinate the City's marketing activities. These individuals should continue the work of the Communications Working Group (CWG) to ensure that organizations charged with promoting San José are working collaboratively and evaluating their efforts to maximize return-on-investment. Prior to development of the Mayor's June Budget Message, CWG members should present a budget for their City/RDA/Airport allocation, along with an overview of their 2010-2011 marketing plan to the group for review and feedback. Funding by the Agency or Office of Economic Development for outside

organizations to conduct marketing/communications or outreach activities shall be reviewed by the CWG along with each departmental marketing plan.

- h. Supporting Clean Tech Companies:** San José has positioned itself as the World Center of Clean Tech Innovation. We have had good success in developing a clean tech cluster by retaining and attracting companies like SunPower, Nanosolar, Solopower, Solar Junction, BioFuel Box and Stion. The City Manager and the Executive Director are directed to continue to pursue opportunities to partner with companies that are successful in receiving Department of Energy loan guarantees in the upcoming months and have the potential of generating many thousands of manufacturing jobs in factories they plan to build in San José.
- i. Small Business Development Program:** Nurturing the success of local small businesses is a strategic goal identified in the 2010-2015 Draft Economic Strategy. While we don't have significant funding for the purpose of growing our small business base, it seems to me that there are currently a few programs that are funded by the City and the Redevelopment Agency. The City Manager and Executive Director should review all separate funds and allocations geared towards small business development programs, and provide a status report back to City Council on the purpose of the programs and the best use of these funds.

## **2. Environmental and Utility Services**

In October 2007, the City Council unanimously adopted the Green Vision for San José, an ambitious 15-year plan to promote clean tech innovation, sustainability, and green mobility. The initiative established 10 bold goals that will help create thousands of new jobs, grow city revenues, expand our local economy and demonstrate how deploying clean and green technology is fiscally responsible.

Within 15 years, the City of San José in tandem with its residents and businesses will:

- 1. Clean Tech** – Create 25,000 Clean Tech jobs as the World Center of Clean Tech Innovation: Venture capital investment in clean technology in Silicon Valley totaled \$1.2 billion in 2009 and \$4 billion for the last three years. There are 4,027 jobs in the core green economy in San José, with energy efficiency, energy generation, and infrastructure accounting for more than three-fourths of those jobs. The City has gained 1,500 new clean tech jobs in introducing dozens of clean tech companies.
- 2. Energy Efficiency** – Reduce per capita energy use by 50 percent: Energy efficiency measures have been implemented at 10 City facilities, and solar panels generating 20 kW of energy at six City facilities have been installed, resulting in a total of approximately \$80,000 in annual savings in electricity costs.
- 3. Renewable Energy** – Receive 100 percent of our electrical power from clean renewable sources: At the end of 2009, 1,554 solar photovoltaic (PV) systems had been installed in San José. Community Development Block Grants (CDBG) funds were used to install

solar PV arrays on three community centers, one library, and two fire stations to generate about 20 kW of energy.

4. **Green Building** – Build or retrofit 50 million square feet of green buildings: Currently, San José has more than 2.1 million square feet of certified public and private green building space, with 15.3 million square feet of green space in design or construction. The New Construction Green Building ordinance became effective in September 2009 and will mandate levels of LEED or GreenPoint Rated certification for certain construction projects.
5. **Waste Reduction** – Divert 100 percent of the waste from our landfill and convert waste to energy: San José has one of the nation's highest diversion rates for apartments and city operations (80%), and one of the highest waste diversion rates of the country's large cities at 66 percent.
6. **Water Conservation** – Recycle or beneficially reuse 100 percent of our wastewater (100 million gallons per day): In 2009, South Bay Water Recycling initiated a \$15 million pipeline expansion program, funded in part by ARRA stimulus grants and \$6.46 million in grants from the Bureau of Reclamation, to add 10 miles of pipe to the existing system.
7. **General Plan** – Adopt a General Plan with measurable standards for sustainable development: The Envision San José Task Force, which meets monthly, developed draft goals, policies, and implementation actions related to sustainable development, and further policy development and discussion are planned for this year.
8. **Emission Reduction** – Ensure that 100 percent of public fleet vehicles run on alternative fuels: Currently 1,042 (41%) of the City's vehicle fleet run on some form of alternative fuel. The fleet size has been optimized and reduced by 1.5 percent in compliance with the City's Green Fleet Policy to allow for the introduction of more fuel efficient vehicles.
9. **Green Street** – Plant 100,000 new trees and replace 100 percent of our streetlights with smart, zero-emission lighting: The iTree-Streets inventory program was used to estimate that there are approximately 242,650 street trees in the City and 87,580 vacant plantable sites that could receive a portion of the 100,000 Green Vision trees. The City has six LED streetlight-deployment projects involving more than 2,000 of the City's 62,000 lights, and once completed, the projects are expected to reduce the City's \$4 million annual streetlight energy bill by about \$130,000 each year.
10. **Trails** – Create 100 miles of interconnected trails: A total of 3.1 miles of trail were added by the end of 2009, and additional projects anticipated to open in 2010 include two reaches of the Penitencia Creek Trail, the Lower Silver Creek/Silverstone Place, and the Guadalupe River Trail from Highway 280 to Willow Street. In 2009, five bike lane projects totaling five miles were completed, with 200 bike racks installed.

Also, in partnership with the mayors of San Francisco and Oakland, I have signed on to the Bay Area Climate Change Compact and adopted a nine-point plan to make the Bay Area the nation's electric vehicle capital.

By capitalizing on our local ingenuity, entrepreneurship and creative talent to solve environmental problems and grow our economy, San José will continue to lead the clean technology revolution taking place across the world.

To continue our environmental leadership, I recommend the following:

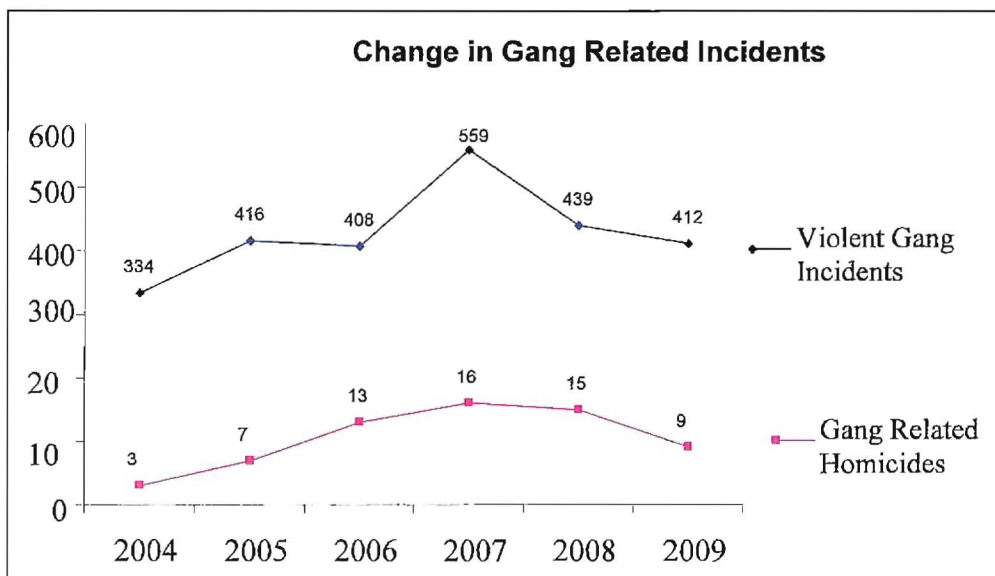
- a. **Recycle Plus SFD (Single Family Dwelling) Solid Waste Services Agreement:** Staff is currently discussing and soliciting proposals for a two-year extension on our current Recycle Plus SFD Solid Waste Services Contract. Staff should consider any and all proposal types such as multi-year extensions as long as they provide high quality, environmentally beneficial and cost-effective solid waste disposal services to the residents of San José. The City Manager is directed to negotiate an agreement with collection and recovery service providers that will maximize revenue for the City, minimize rate increases, and improve service levels for our residents.

### 3. Public Safety and Neighborhood Services

San José is one of the safest big cities in the country. In a recent community survey, residents were asked how safe they feel during the day when walking in their neighborhood, in the city park closest to their residence, and in the Downtown area.

- 92 percent felt safe walking around in their neighborhood.
- 85 percent felt safe walking in the park closest to their residence.
- 71 percent felt safe walking in the Downtown area.

We must continue to ensure that our residents feel safe in their homes and neighborhoods. In our priority setting sessions, we continue to see that public safety is one of the most important city services; public safety continues to be my and the Council's number one priority.



One of our most vital tools in keeping our city safe is the Mayor's Gang Prevention Task Force. The Task Force serves as a national model, and through its collaboration we successfully prevent crime and help at-risk youth



find alternatives to gang involvement. The efforts of the Task Force have helped lead to a decrease in violent gang-related incidents, which is why we must do our best to make gang prevention efforts a priority.

We must continue to work diligently to prevent crime, and although we do not have enough money to do everything we want, we need to continue to make public safety a priority. I recommend the following:

- a. Police Department Reductions:** The City Manager is currently looking at over 100 position reductions in the Police Department to meet current reduction targets. Reductions of this magnitude will have an immediate impact on our community. The City Manager is directed to consider upcoming retirements that are expected to occur over the next several months when looking at reduction proposals. As 9-1-1 emergency response is an essential service, the City Manager should to the extent possible, minimize reductions to patrol.
- b. Civilianization Audit:** In my June 2009 Budget Message, the City Auditor was directed to prioritize an audit to review civilianization opportunities in the Police Department. This audit provides us with the creativity needed to use civilian positions to get officers back on the streets. By hiring civilians to fill positions currently occupied by sworn positions, we can get officers back on the streets and in our neighborhoods. The City Manager is directed to phase these recommendations in this budget and future budgets.
- c. Fire Dynamic Deployment:** Apparatus efficiencies must be taken into consideration and analyzed for cost reductions. The City Manager is directed to review opportunities for a dynamic deployment plan for the Fire Department. Dynamic deployment is a strategy that relies on historical service demand data to identify core fire station locations from which to redeploy available resources at various levels of availability.
- d. Consolidating Gang Services:** Our gang prevention efforts have had large successes since their inception. To help preserve our gang prevention efforts, we must search for opportunities to consolidate and become more efficient. Because of the budget cuts, staff is directed to audit the allocation of funds made within the Mayor's Gang Prevention Task Force to seek possibilities for consolidation. We must also consider programs operated through the Strong Neighborhoods Initiative and the Police Department.

There are currently 22 community based organizations and 35 positions that are funded through Bringing Everyone's Strengths Together (BEST). The City Manager is directed to examine the use of funds and report back any possibilities of consolidation or reductions, specifically which positions could be eliminated and which services could be consolidated to reduce the amount of grant dollars given.

- e. Safe Summer Initiative:** The Safe Summer Initiative has been a resounding success. Approximately 5,500 participants received over 4,000 hours of activities funded by the Safe Summer Initiative in summer 2009. The 45 contracted agencies provided approximately 40 activities throughout the summer. From the summers of 2007 to 2009,

there has been a 25 percent decrease in overall gang crimes and a 26 percent decrease in violent gang crimes. This program does not have funding this year; however it is a program that has proven results and I recommend that \$250,000 be allocated from anticipated unallocated BEST funds.

- f. **Independent Police Auditor (IPA):** The IPA delivers services to and works within the Public Safety CSA. Therefore, the IPA will be assigned to the Public Safety CSA and will have to meet the Public Safety CSA reductions.
- g. **Crossing Guards:** The safety of our school children remains a top priority for San José residents, as well as the City Council. During meetings with superintendents at the Schools/City Collaborative, the superintendents stated that this was the most important service the City provides for the schools and is their number one priority. The City Manager is directed to minimize impacts to the elementary school crossing guard program and report back on the crossing guard recommendations made in last year's Budget Message. This includes the installation of pedestrian-activated crosswalks at unstaffed middle school intersections, use of trained volunteers, implementation of cost-effective programs that are in place in other jurisdictions, exploration of alternate funding sources such as state and federal grants, and working with the Schools/City Collaborative to find solutions to ensure the safety of our children.
- h. **Healthy Neighborhood Venture Fund (HNVF):** The Anti-Tobacco Master Settlement Agreement (MSA) funds have provided valuable funds to improve the quality of life of San José's youth and senior populations through the Healthy Neighborhoods Venture Fund program. To best preserve basic levels of core City programs and services to these vulnerable populations, the City Manager is directed to maintain funding for the Children's Health Initiative and use the average non-public safety CSA reduction as a guide for reduction proposals to the HNVF competitive grant funds.

#### 4. Transportation and Aviation Services

The City of San José Transportation and Aviation Services City Service Area works with other agencies – local, state, and federal – to provide a safe and efficient transportation system dedicated to developing and improving the city's freeways, transit, streets, sidewalks, parking facilities, bicycle facilities, and the Airport and its support facilities. Together, the transportation system supports San José's livability and economic vitality.

The CSA is faced with the difficult challenge of operating on a reduced budget while undertaking aggressive capital programs, including the following:

- **BART Extension through San José to Santa Clara:** The \$6.1 billion, 16.1-mile BART line includes the federal 10.2-mile Silicon Valley Berryessa extension and the additional 5.9 miles to Diridon Station. The VTA Board intends to connect BART to Caltrain and the future high-speed rail at Diridon Station, thereby forging a local connection to the East Bay. An estimated 46,460 riders are expected to ride the Berryessa extension daily, plus an additional 52,290 riders when the full project is completed. It is projected that the

project will attract \$6 billion in economic benefits to the area, among other environmental benefits.

- **High-Speed Rail:** The project to connect Los Angeles to San José and San Francisco will include the construction of four new tracks at the San José Diridon Station, as well as a crossover between Davis and Sacramento to improve trip times and reliability. The City Manager and Executive Director are directed to work together to ensure that the design for high-speed rail is beneficial to San José.
- **Automated Transit Network:** The City of San José, in partnership with the Valley Transportation Authority, plans to build the nation's first Automated Transit Network (ATN) to connect Caltrain, Light Rail, and the future BART systems to the Norman Y. Mineta San José International Airport and eventually to other parts of the city. Construction of the environmentally friendly system of non-stop, computer-controlled vehicles could begin in 2013, with consulting work to start this spring.
- **Local Streets and Roads:** In a report by the California Statewide Local Streets and Roads Needs Assessment, which surveyed 58 counties and 478 cities in California during 2007-2008, it was determined that the statewide average roadway Pavement Condition Index (PCI) is 68, which falls within the "at-risk" range on a scale of 0-100. San José's PCI is 64, while the average PCI for all Santa Clara County jurisdictions is 70. San José's score indicates that local roads are nearing a point of rapid deterioration possibly requiring more to maintain or rehabilitate.

According to the Department of Transportation's annual review of the City's transportation infrastructure conditions and funding needs, San José has a one-time, \$249 million backlog of street and roadway maintenance needs. These include 404 miles of roads in poor or failed condition (<50 PCI) in need of resurfacing, and 794 miles in acceptable or better condition. An additional \$145 million backlog of other essential street components brings the total backlog to \$394 million.

**Norman Y. Mineta San José International Airport:** The opening of the new Terminal B baggage claim carousels in early February cleared the path for the closure and demolition of the Airport's Terminal C baggage claim building to make space for the completion of the new loop roadway. The construction of Terminal B and the Terminal B Concourse is part of the Airport's \$1.3 billion improvement and modernization program, to which the Transportation Security Administration (TSA) has awarded more than \$20.9 million for a state-of-the-art baggage screening system in Terminal B. The Airport also received \$20.6 million from TSA for Terminal A improvements last year. In August 2009, the Federal Aviation Administration also awarded \$5.2 million to the Taxiway W Phase I Improvements project, which is approximately 75 percent completed.

In June, San José will open its \$1.3 billion airport, under budget and on schedule. It will be a world-class airport which will offer business and leisure travelers a truly superior experience. But the national financial and economic crisis, higher energy and regulatory costs, and the impending payments associated with debt service have and will continue to

take a toll on the competitiveness of the airport. Every effort must be taken immediately to turn this situation around and assure that our airport regains the traffic it experienced before the dot-com bust and effectively competes with airports throughout the Bay Area, the U.S., and the world.

The City Manager is directed to return to the Rules Committee in four weeks with a work assessment analysis, as well as a timeline to bring to Council a five-year strategic plan that will keep the airport competitive in our market. Each of the proposals offered by staff must be carefully evaluated from a cost-benefit perspective, and special attention paid to the impacts of proposals that would have an effect on the quality of life of our residents and workers. I also recommend that the plan include a business development strategy and a comprehensive community and stakeholder outreach and engagement program for each of the proposals being evaluated as appropriate.

## 5. Strategic Support

I recommend the following for the Strategic Support CSA:

- a. **Employee Suggestion Program:** The employee suggestion program is close to being launched under the title “E-Ideas: Suggestion and Innovation Program.” The web-based program encourages City employees to log onto a website through the City’s Intranet page with their employee number in order to submit their suggestions, vote or comment on ideas, and collaborate. Ideas are organized into categories including “improving productivity,” “reducing costs and expenditures,” and “providing a safer work environment.” Given the City’s fiscal situation, there are no financial incentives for participating in the program. The City Manager is directed to review the effectiveness of the program after six months and report back to City Council during the mid-year budget process regarding the need to add financial incentives.
- b. **Employee Wellness Program:** A results-focused Employee Wellness Initiative implemented a number of programs during a two-year pilot period, including Worksite Wellness screenings; MedExpert Individual Medical Decision Support Service to provide information on medical conditions, treatment or prescription options; health plan reward programs encouraging employees to participate in wellness programs for monetary compensation; on-site smoking cessation classes; and the Annual Employee Wellness Conference and Fair. The cost to provide health care benefits to City employees and retirees in 2009 was \$107.4 million dollars. The City Manager is directed to work with department managers to facilitate employee participation in Employee Wellness Program activities and events through improved communication and other practices.
- c. **Workers Compensation:** A 2008 consultant report estimated that the City pays \$1.7 million per year by not offsetting Police and Fire disability retirement pension benefits when disability benefits are paid. The City Manager is directed to continue to pursue structural changes to the City’s Workers’ Compensation Program that would include but not be limited to: 1) reducing the City’s policy of providing up to nine months of disability leave supplement pay at 85 percent for non-sworn; and 2) implementing a



retirement benefit payment offset for sworn employees receiving disability retirement payments that replicates the offset for retired non-sworn employees.

- d. **Reduce Medical and Dental In-Lieu Cash Payments:** The Health In-Lieu Plan is an optional benefit plan that allows employees to forgo City-provided medical coverage in exchange for cash. It is estimated that if the City reduced its in-lieu payout from 50 percent to 40 percent of the City's contribution rate to medical premiums, the City could save \$1 million per year; or if the City were to reduce its in-lieu payout to 30 percent of the City's contribution rate, the City could save \$2 million per year. It should be noted that as premiums of City-sponsored medical plans rise, so do the potential savings from reducing the in-lieu payout. The City Manager is directed to continue discussions with our bargaining groups as a potential cost saving strategy.
- e. **Retiree Healthcare Reimbursement In-Lieu Program:** It is estimated that there are potential significant savings in the first year of a retiree in-lieu program. Such a program could also improve the City's projected long-term retiree healthcare liability, potentially impacting long-term retiree health care contribution rates. The City Manager is directed to explore a reimbursement program for qualified City retirees who suspend their medical benefits as part of the retiree healthcare reform.
- f. **Sick Leave Payouts:** Memorandum of Agreements allows for police and fire staff to receive 100 percent payout of unused sick days at retirement; all other bargaining groups receive 75 percent of a maximum of 1,200 hours at retirement. The rise in personnel costs has led the City to examine all ways to reduce future expenses. The City Manager is directed to continue discussions with our employee groups on options to lower these costs.
- g. **Medical Benefit Cost Containment Strategies:** There are potentially \$16.8 million in cost containment strategies including:
  - Potential savings of \$4 million per year by increasing the employee's share of medical premiums from a 90/10 to 80/20 employer-to-employee contribution ratio.
  - Potential savings of \$10 million per year by introducing a lower cost deductible plan.
  - Potential savings of \$2.8 million per year by increasing co-pays from \$10 to \$25 for most covered employees.

The City Manager is directed to pursue the aforementioned cost containment strategies.

- h. **Essential Services Preservation Fund:** The City Manager is directed to set aside \$500,000 of one-time funds that may be used for the purpose of supporting services that are of essential importance to the residents. Services deemed essential by the City Council may be maintained with the use of one-time funds.
- i. **City County Collaboration:** Santa Clara County and the City of San José each currently provide a range of municipal type services to residents and businesses. Considering the proximity of the unincorporated area of Santa Clara County to the City of San José and

the common interest providing effective and efficient high-quality services, there may be an opportunity to collaborate on select services and maintain or improve the quality of service at a lower cost. The City Manager is directed to work with the County Executive to evaluate the collaboration of services and determine whether an opportunity to collaborate exists and report back to City Council. Topics and areas to review are General Services, Human Resources, Housing Services, Parks, Information Technology, Public Affairs, and Public Safety.

- j. Policy and Process Review:** Direct the City Manager to return to the City Council during the May Budget Study Sessions with a list of existing Council policies, budget policies, or processes which: limit the City Manager's ability to control escalating costs or reduce expenditures; involve processes that are too long or costly for the City Manager to implement in time for the presentation of the Fiscal Year 2010-2011 Budget; increase the cost of doing business as a contractor to the City of San José; inhibit the City from attracting businesses, small or large, from starting or expanding in the City of San José; and inhibit the ability of appropriate development from moving forward immediately.
- k. City and Agency Travel:** Due to the unprecedented budget situation, the City Manager, the Council Appointees, and the Executive Director are directed to reduce travel costs. Travel to meetings and conferences in-state and out-of-state should be reevaluated to ensure that they are vital to city business and necessary.
- l. Beyond Budget Cuts:** In June 2008, after conducting an organizational assessment of functions at City Hall, the City Manager launched the "Beyond Budget Cuts" initiative, a coordinated effort toward organizational improvement in cooperation with management, labor, and employee representatives throughout the City of San José. Five "Action Teams" have thus far created a report draft on long-term IT investment priorities; recommended amendments to contract authority limits; streamlined overly complicated purchasing rules and travel policies; and procured the Medici Innovation Training curriculum to offer training classes. Since the initiative began in 2008, the City has allocated \$150,000 in one-time funds for the overall initiative and \$25,000 in annual funds for the Employee Suggestion/E-Ideas Program. The City Manager is directed to continue these types of initiatives to encourage innovation that will enable employees to assist in the response to budget challenges to the City.
- m. Pension Obligation Bonds:** The City Manager is directed to analyze the benefits and drawbacks of issuing pension obligation bonds, and report to City Council during the budget process.
- n. Construction and Conveyance Tax Revenues:** The City Manager is directed to analyze bonding against future Construction and Conveyance Tax revenue as a source of potential funds to help with our budget shortfall, and report back to City Council during the budget process.

- o. Price Reductions from Private Vendors:** The City Manager, to the greatest extent possible, is directed to explore every opportunity to seek temporary price concessions with vendors, whether existing contracts are open or not.
- p. Agency/City Support Services:** It is anticipated that there will be a decline in funding from the Redevelopment Agency for City support services for 2010-2011. Funding levels for support services will be refined and updated based on discussions between the City and Agency. To avoid increasing the already substantial General Fund shortfall projected for 2010-2011, any reduction in Agency reimbursements should be accompanied by a corresponding reduction in City support costs.
- q. Deferral of Committed Additions:** The City Manager is directed to defer any avoidable committed additions in this year's budget. The deferrals should include the City Council approved addition of 25 police officers in 2010-2011 and the opening of any new facilities that would increase operating and maintenance costs.
- r. South San José Police Substation:** The City Manager is directed to defer the opening of the police substation from March 2011 to September 2011. As costs continue to present challenges to the General Fund shortfall in 2010-2011 and are anticipated in future years, a continuation of the City Council-approved strategy to defer or delay the opening is required. This six month deferral will achieve savings in facility operating and maintenance costs of approximately \$1.4 million in 2010-2011.
- s. Administrative Services Hub:** The City Manager is directed to review and report back on the concept of an administrative services "hub" for accounts payable, timekeeping and routine purchasing/contract negotiations as a cost-saving measure.
- t. Temporary Assistance to Needy Families (TANF) Stimulus Funds:** The City Manager is directed to explore any opportunities to use TANF related stimulus funding for job-stabilization and creation measures.

## **6. Preparing for Fiscal Year 2011-2012**

If we cover the \$116 million shortfall for 2010-2011 with all ongoing solutions, we still face a deficit of \$20.1 million for 2011-2012. There are actions we can start now that could avoid layoffs and service reductions in 2011-2012. The City Manager is directed to evaluate the following and report back in the fall:

- a. Dolce Hayes Mansion and Convention Center:** Revenues for the year ending June 30, 2009 were \$12.6 million, a decrease of approximately 21 percent from its budgeted amount. More than \$9 million in contributions were made from the General Fund in 2008-2009, including the Council-approved \$5 million to pay the outstanding principal balance on the Center's Comerica basic line of credit and term loan agreement in 2008, and \$4.1 million to assist the Center in making debt service payments. In 2009-2010, the City's General Fund subsidy is expected to total \$2.7 million due to a one-time offset from related debt service savings. For 2010-2011, the Center's General Fund subsidy is

projected to increase to \$5.9 million annually. The City Manager is directed to explore options for selling the property including at what price level its debt service would be eliminated, in order to dramatically reduce annual costs.

- b. San José Municipal Water:** Discussions around selling San José Municipal Water have taken place for more than nine years. Currently the City does not get a rate of return or in-lieu fees from the system. If sold, the City's General Fund could receive ongoing property tax and utility tax, proceeds from the sale or lease, or franchise fee revenues. The City Manager and the Environmental Services Department are directed to reevaluate the feasibility of leasing Municipal Water to private companies that could generate millions of dollars of revenue for the City, as well as current alternatives to generate a rate of return on the system.
- c. Municipal Golf Courses:** In 2008-09, activity at Los Lagos Golf Course was down approximately 17 percent, resulting in a decrease of \$52,000 in revenue from the previous year. Rancho Del Pueblo Golf Course saw a 10 percent increase in activity from the year before, which was attributed to the success of its First Tee of San José youth program. A transfer of \$1 million in General Fund subsidies was deposited into the Municipal Golf Course Fund in 2008-2009, but it was recommended that the operating subsidy appropriations be increased \$50,000 for Los Lagos and \$75,000 for Rancho Del Pueblo. The City has contributed more than \$400,000 since the 2000 opening of Rancho Del Pueblo, which has had only one profitable year of operation (2001-2002). The City Manager is directed to perform property valuations and to review possible rezoning and sale of Rancho Del Pueblo in order to eliminate the debt service and allow our golf courses to operate without a General Fund subsidy.
- d. Former City Hall Lot E:** In the 2007 Land Use and Economic Analysis Study, which examined various development scenarios for the former City Hall and the Lot E, it was reported that the Lot E could generate significant one-time funds. The City Manager is directed to perform property valuations and to review the possible rezoning and sale of Lot E.

## **7. General Fund Structural Deficit Elimination Plan**

Given the severity of the General Fund budget shortfall for 2010-2011, the City Manager did not revise the General Fund Structural Deficit Elimination Plan (GFSDEP), which was last updated in February 2009, as part of the 2011-2015 Five-Year Forecast. The City Manager is directed to bring the GFSDEP to Council with the release of the next Five-Year Forecast update.

While the plan will be updated after the extensive budget actions necessary to balance the current budget are approved, it should be noted that a number of the strategies outlined in the General Fund Structural Deficit Elimination Plan are being pursued as part of the 2010-2011 budget process.



These strategies include:

- The continuing implementation of the asset management program.
- The card room ballot measure.
- Economic development incentives.
- Optimization and service delivery model reviews.
- Reducing the rate of increase in personnel costs.

Several of the proposals to reduce the rate of increase in personnel costs are subject to the meet and confer process and are being pursued during contract negotiations with the City's bargaining units. Given the necessity to ensure long-term sustainability of the City's cost structure, the City Manager is directed to accelerate pension/retiree healthcare reform.

The projected General Fund Structural Deficit has been updated to reflect revised revenue and expenditure projections in the 2011-2015 General Fund Forecast and revised unmet/deferred infrastructure and maintenance needs costs.

A few things to point out regarding the unmet/deferred infrastructure and maintenance needs costs:

- The City does not include the \$8.1 million (an annual installment to build within five years to the \$40.7 million needed annually) it would take to adequately maintain its infrastructure and maintenance backlog which consists of mostly street maintenance. Due to the City's inability to completely fund replacement and renewal projects, this number has grown by \$2.2 million since November 2008.
- The annual figure does not include \$9.75 million for sidewalk, curb/gutter, and tree maintenance that are the responsibility of property owners.
- The City's five-year forecast does not address one-time infrastructure and maintenance needs of \$446 million in the General Fund (\$821 million inclusive of all funds).

Based on these revised projections, the General Fund structural deficit is expected to total approximately \$222.3 million over a five-year period as shown in the following table:

**2011-2015 General Fund Structural Deficit Projection (February 2010)**  
(\$ in Millions)

	2010-2011	2011-2012	2012-2013	2013-2014	2014-2015	Total
<b>Projected Base Shortfall (Feb 2010 Forecast)*</b>	(\$116.2)	(\$20.1)	(\$18.0)	(\$21.5)	(\$5.8)	(\$181.6)
<b>Unmet/Deferred Infrastructure &amp; Maintenance Needs**</b>	(\$8.1)	(\$8.1)	(\$8.1)	(\$8.2)	(\$8.2)	(\$40.7)
<b>Total Incremental Deficit</b>	<b>(\$124.3)</b>	<b>(\$28.2)</b>	<b>(\$26.1)</b>	<b>(\$29.7)</b>	<b>(\$14.0)</b>	<b>(\$222.3)</b>
<b>Total Cumulative Deficit</b>	<b>(\$124.3)</b>	<b>(\$152.5)</b>	<b>(\$178.6)</b>	<b>(\$208.3)</b>	<b>(\$222.3)</b>	<b>(\$222.3)</b>

\* Funding for cost-of-living (COLA) salary increases not factored into the Forecast unless there is an approved contract agreement. For this Forecast, 2% COLAs are assumed for the Municipal Employees' Federation and Confidential Employees' Organization in 2010-2011 only. The Forecast includes committed additions previously agreed upon by Council, such as the addition of 25 Police Officers in 2010-2011 and 2011-2012 (50 total) and operating and maintenance funding for capital projects coming on line.

\*\* Does not address one-time needs of \$446 million in the General Fund (\$821 million all funds).

## **REDEVELOPMENT AGENCY BUDGET PROCESS**

Unfortunately, the Redevelopment Agency finds itself dealing with numerous unresolved factors that could impinge on its ability to stimulate economic growth, job creation, affordable housing, and neighborhood improvements. Uncertainties in the financial markets could impact short-term borrowing. The State Of California, which has already taken \$75 million from the Agency, might attempt to take even more money. Payments to Santa Clara County still need to be renegotiated.

Additionally, the County Assessor will take the unprecedented action of *lowering* the base year assessed values of nearly every property in the state by 0.237% and San José Redevelopment tax increment is projected to remain flat. This is yet another uncertainty for the Agency – the actual amount of tax increment revenue from project areas will not be known until the County Assessor closes the roll in late July. In light of the Agency's need to fund its operations until the actual revenue base is known, I recommend the Agency submit its Fiscal Year 2010-2011 Proposed Capital and Operating Budget on May 3, 2010, followed by a revised Fiscal Year 2010-2011 Capital Budget and Fiscal Year 2011-2015 Capital Improvements Program on August 31, 2010.

## **CONCLUSION**

This Budget Message presents us choices. We can lead San José into a healthy fiscal state or we can maintain business as usual and continue to cut services and layoff valued employees. Making tough choices isn't easy, but neglecting to provide leadership is far worse. Through the community based budgeting process, we now know which services residents truly value. Together, we can implement community priorities, maintain core services, stimulate the economy, and reduce layoffs.

We should be proud of our many accomplishments over the past few years that have made San José a great place to live, work and raise a family. San José is a community that our residents are proud to call home. Despite the current economic challenges facing the region, state, and nation,

I am confident we will continue to find solutions to achieve our community's goals and provide the quality services that our residents deserve.

**COORDINATION**

This memorandum has been coordinated with the City Manager, City Attorney, and Redevelopment Agency Executive Director.